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SUBJECT: SMER LACKS DIRECTION ON ECONOMY

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Classified By: Ambassador Rodolphe M. Vallee for Reasons 1.4 (B) and (D)  
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11. (C) SUMMARY - The recent release of Smer's official election program sheds little light on what the economic policy would actually look like in a Smer-led coalition government. The party platform is essentially a critique of the reforms instituted over the past eight years, and calls for an overhaul of key tax, healthcare and other reforms that Smer claims have damaged Slovakia's "social character." Despite the strong campaign rhetoric, it is clear that Smer lacks the analytical capacity to institute the reforms, let alone costing out the budgetary implications. The party would likely turn to former HZDS and SDL officials to fill key economic positions in a new government. In addition, many suspect that the top Smer financial backers, most of whom have ties to Meciar-era business deals, would not support the introduction of new taxes on individuals and corporations. End Summary.

-- ECONOMIC PROGRAM, AS PRESENTED TO VOTERS --

12. (SBU) Smer's election program is primarily a critique of the current ruling coalition's economic reforms, arguing that these reforms have benefited the rich but have not improved conditions for the majority of the population in Slovakia. Fico has stated that the combination of tax cuts, increased labor market flexibility and reduction in social benefits (welfare, health care and pensions) has had a negative impact on the average Slovak worker and goes against "the social character of Slovakia." After having "floated" a number of possible economic reforms since last fall, Smer came out with an official election program in mid-May that would reverse several of the reforms instituted by the current government.

13. (SBU) Smer's top priority is also the most controversial - reforming the tax regime. Smer proposes introducing a progressive income tax with a top rate of 25 percent for those earning more than 600,000 SKK (USD 20,500), with a standard rate of 19 percent and a lower rate for those at the bottom of the economic ladder. The program calls for a two-tiered value-added tax (VAT) which would introduce a lower rate on basic foodstuffs, medicines, social services, books, energy, water and internet services. Although the corporate rate would remain a flat 19 percent, Smer plans to create a special, higher rate, tax regime for "natural monopolies, dominant firms, and financial and banking institutions." It would also like to reintroduce both a tax on dividends and a "gift tax." Given the fame of the Dzurinda government incentives for new investment, the combination of such measures by Smer would discourage some new investors from coming to Slovakia.

14. (SBU) After taxes, Smer's top priority is undoing several of the healthcare reforms by eliminating user fees for health services and re-establishing public health insurance for all

(Reftel A). Additional "social" proposals include loans for newly married couples, an increase in the allowance for newborns, introduction of a "Christmas allowance" to pensioners, and a promise to not introduce tuition for university students. Smer vice-chairman Pavol Paska told us that Smer would also overturn the recently-approved healthcare legislation that increases patent protection by providing a linkage between the drug authority and the patent office. Smer would ask the namebrand pharmaceutical companies, the generics and the government to reach a new compromise. In addition, Smer would review all privatization decisions made by the current government and would not hesitate to cancel contracts that have breached the law.

¶5. (C) Fico officially supports the current plan for Slovakia to adopt the Euro by January 1, 2009. Privately, however, his advisors say that fulfilling Smer's spending priorities on important social programs is of greater importance than maintaining this deadline. Peter Mihok, who is considered a top candidate for an economic ministerial post (see para 8.), noted that Fico would likely delay Euro introduction until after the 2010 parliamentary elections to avoid any negative associations with voters.

-- THE PERSONALITIES BEHIND THE POLICIES - GOING BACK IN TIME TO FILL TOP POSTS --

¶6. (SBU) Determining what economic policies a Smer-led government would focus on is complicated by the party's lack of depth and expertise on economic issues. Smer MP Igor Sulaj authored the party's first economic program back in November, and had initially been mentioned as the top candidate for Finance Minister. Although he was heavily criticized from both within and outside of the party for

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putting forward "populist" proposals that "did not add up," Smer's final election program is remarkably similar to Sulaj's original proposals. Nevertheless, Sulaj is still considered more likely to end up as Chairman of the Tax Directorate instead of in a top ministerial position. Fico has appeared reluctant to use Sulaj as a regular spokesman on economic issues. In addition, Sulaj has some background in tax issues and comes from Banska Bystrica, where the Tax Directorate is located.

¶7. (C) Those mentioned as "top advisors" to Fico and potential ministerial candidates generally come from outside of the party and are former Movement for a Democratic Slovakia (HZDS) and Slovak Democratic Left (SDL) members. We have also heard that Fico has borrowed advisors from the Czech Social Democratic party (CSSD) to help develop his economic program. The lack of internal experts who could speak on behalf of the party was evident from the American Chamber of Commerce's unsuccessful efforts to get Smer to participate in its series of breakfast meetings with top economic advisors from each of the main political parties. Smer was the only party that did not participate, in large part because Fico was out on the campaign trail and the party lacks experts who could competently discuss and defend their program.

¶8. (C) Some of the names who are most frequently mentioned as playing an important role in the Smer-led government include:

- Peter Mihok is the Chairman of the Slovak Chamber of Commerce and was formerly associated with SDL. Mihok has been mentioned as a "hot candidate" for Minister of Economy, and in a conversation with Econoffs made it very clear that he had been in regular touch with Fico throughout the campaign. Mihok is outwardly supportive of "social democratic" policies, but noted that many of Fico's campaign proposals would need to be moderated if Fico forms the next government.

- Jozef Brhel was Deputy Economy Minister under Meciar from

1995 to 1998, and later served as an MP for HZDS. He left Meciar's party and became an independent MP in 2002 during the last parliamentary session, and left parliament altogether in 2004. Brhel is one of the main financiers of Smer (see Para 9 below), and is close to Smer's shadow economic minister, Maros Kondrot. Reliable contacts in the banking sector with connections to Smer tell us that Brhel is currently Fico's top choice to be finance minister. (Note: Kondrot is generally considered a more likely candidate for Deputy Secretary, especially if Brhel is Minister).

- Peter Stanek is a researcher at the Prognostic Institute at the Slovak Academy of Science. He worked in the early 1990's as Meciar's top economic advisor and later as deputy finance minister under Meciar from 1994 to 1998. Stanek has been rumored as a likely candidate for Finance Minister, but he recently told us that he is no longer advising Fico and has decided to stop working with any of the political parties in the election campaign. Stanek noted that he does not support many of the policies outlined in Smer's economic program, especially the tax proposals, and thinks that Fico will have a difficult time finding competent candidates to fill key ministerial roles.

- Dusan Munko, a Smer MP from Bratislava, is a possible candidate for Minister of Economy. A former agent of StB, the communist secret police, Munko privatized the largest Slovak travel agency, Satur, and has interests in several other businesses in Bratislava. His daughter, Norika Federova, is the CEO of Satur and is married to the head of the investment banking division of J&T Associates, the controversial private equity company.

- Slavomir Hatina was behind the Meciar era privatization of the Slovnaft refinery, which he later sold to the Hungarian oil company MOL. He is not currently connected with any political parties.

-- SMER INC.: BUSINESS INTERESTS TO HAVE A VOICE IN POLICYMAKING --

19. (C) Many political observers consider Smer's economic program to be nothing more than election promises, believing that economic policy will be dictated more by business interests who are alleged to be the main supporters of the party. The Ambassador has heard from more than one credible source such extreme comments as "If Fico doesn't form the next government, his life will be in danger, because the shady money behind him will not be pleased." Several newsmagazines, including Tyzden and the Slovak Spectator, have run articles describing Smer as a joint-stock company, in which the "shareholders" will have significant influence

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on policy decisions. These supporters are primarily made up of businessmen who got rich from their government connections during the Meciar-era. These include several former HZDS MPs who split from the party in 2002 such as Ivan Kino (Director of Slovenska Sporitelna under Meciar), Jan Gabriel (former Director of VUB in the 1990s), Vladimir Poor (who privatized Nafta Gbely) and Jozef Brhel (see Para. 8). Fedor Flasik, who was head of the Donar advertising agency during the Meciar governments, has lost some influence in recent months due to a dispute with Fico.

10. (C) COMMENT - The business community is taking a wait and see approach towards the economic program of a Smer-led government. The general view is that Fico will say anything to appeal to voters and will have to be much more pragmatic if he is able to form a government and controls several of the key economic ministries. He will also have to work with coalition partners who will be less willing to turn back the clock. The bigger concern is the lack of sound, forward-looking economic advisors who understand the economic issues as well as the importance of maintaining the business-friendly approach that has been a key element of

Slovakia's success in recent years. If investors invest "on the margin", i.e., comparing today to what they had yesterday and can expect tomorrow, they may see even a marginally less business-friendly government as reason to look elsewhere in the region.

VALLEE